CONNELL & ANDERSEN LLP
545 FIFTH AVENUE
NEW YORK, NEW YORK 10017

WILLIAM F. CONNELL
ROY C. ANDERSEN

TELEPHONE: (212) 687-6900
FACSIMILE: (212) 687-6999
randersen@connellandersen.com

OF COUNSEL
GEORGE A. SCHNEIDER
LUCA CANTELLI

November 26, 2012

<u>Update on FATCA Requirements for Foreign Banks</u>

What is FATCA??

U.S. taxpayers unfortunately hide money and earnings outside the U.S. to avoid paying taxes. The Foreign Account Tax Compliance Act was adopted to crack down on this practice. Thus foreign financial institutions including banks have the "option" of entering into agreements with the IRS to disclose certain information regarding their U.S. customers. Those foreign financial institutions that opt not to sign agreements will face 30% withholding taxes on certain payments made to the foreign financial institutions from the U.S.

What is the current status of FATCA?

FATCA implementation has been slower than originally contemplated. The IRS rules are still in proposed form and only one IGA (see below) has been signed as of this date. Nonetheless, FATCA is still looming and it has serious consequences for banks that do not comply; most serious is the potential 30% withholding tax. While the IRS likes to paint FATCA as a disclosure rule, it requires due diligence, then regular compliance with the various governance and policies and procedures to insure that ongoing reporting is done accurately and on a timely basis.

What should you be doing about FATCA??

It is hard to generalize about what foreign banks should be doing about FATCA at this moment. I am aware that some banks have organized FATCA teams and are actively looking at steps to comply. Some banks have hired consultants to assist the bank with workflows, policies and software fixes to reflect the items that will most likely be required. Many banks are doing very little and are waiting to see how things will sort out and will either engage in a fire drill approach to compliance or hope that deadlines will be extended.

Why governments will likely sign cooperation agreements with the U.S. to save their financial institutions from the FATCA nightmare

Under FATCA, foreign governments may sign intergovernmental agreements ("IGA"s) with the US, which on a government to government basis make life easer for foreign financial institutions by reducing disclosure, easing conflicts with foreign home country laws and avoiding the burdens of the pass through withholding obligations. The US and the UK have signed an IGA and numerous other countries are in the process of considering whether to sign up. A bank located in such a country will likely not be subject to FATCA withholding on their receipts, nor required to impose it on outbound payments.

What about banks in countries that are not going to sign IGAs with the U.S.?

It is a safe bet that not every country will get around to signing an IGA with the US. Banks in those countries will have to deal with having to sign a separate agreement with the US IRS or deal with pass through withholding on payments to them from other FATCA compliant foreign financial institutions and a 30% withholding on US source payments to them. Even if they sign an agreement with the IRS, these banks will still have to make pass through withholding on payments.

Certain things were "grandfathered" and what does this mean?

Most foreign financial institutions had been proceeding on the assumption that many of their activities prior to January 1, 2013, would be grandfathered and thus never subject to FATCA withholding. These activities included loans, derivatives, debt securities and other obligations advanced or committed prior to that date. The IRS recognized that the grandfathering date was not realistic given the lack of guidance on important parts of the law, and thus the IRS recently pushed back the implementation of certain aspects of FATCA:

- Any withholding of US source payments will start on January 1, 2017 (instead of January 1, 2015);
- Grandfathering against pass through withholding will be extended for at least six months after FATCA regulations are finalized;
- The timetable for due diligence and other compliance burdens will not be required until January 1, 2014

In general, what accounts have to be reviewed?

Preexisting Accounts of Individuals

Foreign financial institutions will have to identify U.S. accounts, which include both accounts held by U.S. individuals and certain U.S. entities, and accounts held by foreign entities with substantial U.S. owners (generally, owners with a greater than ten percent interest).

Preexisting individual accounts with a balance or value that does not exceed $50,000 are exempt from review.

Accounts that are offshore obligations with a balance or value that exceeds $50,000 but does not exceed $1,000,000 are subject only to review of electronically searchable data.

Accounts with a balance that exceeds $1,000,000 are subject to review of electronic and non-electronic files for U.S. indicia, including an inquiry of the actual knowledge of any relationship manager associated with the account.

Preexisting Accounts of Businesses

Preexisting entity accounts with account balances of $250,000 or less are exempt from review until the account balance exceeds $1,000,000. Foreign financial institutions can generally rely on AML/KYC records and other existing account information to determine whether the entity is an FFI or is a U.S. person.

New Accounts of Individuals

Foreign financial institutions will be required to review the information provided at the opening of the account, including identification and any documentation collected under AML/KYC rules. If U.S. indicia are identified as part of that review, the FFI must obtain additional documentation or treat the account as held by a recalcitrant account holder.

In general, what information has to be reported?

Foreign financial institutions will be subject to phased-in reporting requirements. These requirements will likely remain the same but the timetables for reporting will likely change due to the delays in implementing FATCA.

For the first two years of reporting, foreign financial institutions will have to report only name, address, TIN, account number, and account balance with respect to U.S. accounts.

Beginning with reporting in the third year, in addition to the aforementioned information, income associated with U.S. accounts must be reported.

Beginning with reporting for the fourth year, full reporting of information will be required.

R.C.A.